

Message Text

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TO SECSTATE WASHDC PRIORITY 8568
AMCONSUL MONTREAL
INFO ALL OTHER CONSULATES IN CANADA POUCH

UNCLAS SECTION 01 OF 02 OTTAWA 04359

PASS CEA, TREASURY, FRB

E.O. 11652: N/A
TAGS: ECON, EFIN, CA
SUBJECT: ECONOMIC DEVELOPMENTS: WEEK ENDING SEPTEMBER 1

REF: OTTAWA 4213, 4230 AND 4249

1. SUMMARY: CANADIAN DOLLAR EXCHANGE RATE SAGGED UNDER CONTINUED SELLING PRESSURE. OFFICIAL BATTLE TO SUPPORT EXCHANGE RATE WAS COSTLY IN AUGUST AS RESERVES DECLINED BY NEARLY USDOLS 400 MILLION TO U.S. DOLS 4.2 BILLION DESPITE USDOLS 300 MILLION DRAWDOWN OF GOC'S LINE OF CREDIT WITH U.S. BANKS. GOC ANNOUNCED DETAILS OF CUTS IN UNEMPLOYMENT COMPENSATION AND JOB CREATION MEASURES PREVIEWED BY FINANCE MINISTER CHRETIEN. REAL GNP GROWTH ACCELERATED TO 4.4 PERCENT ANNUAL RATE IN SECOND QUARTER FROM FIRST QUARTER RATE OF 2.9 PERCENT. FEDERAL/PROVINCIAL TASK FORCE ON TOURISM CITED HIGH COSTS AND GOVERNMENT REGULATION AS CONTRIBUTING TO MOUNTING CANADIAN TRAVEL DEFICIT. WHOLESALE FOOD PRICES DECLINED IN JULY, HELPING TO MODERATE RISE INTERNAL INDUSTRY SELLING PRICES. INCREASE IN UNCLASSIFIED

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EMPLOYMENT, EARNINGS AND HOURS WORKED CONTRIBUTED TO RISE IN LABOR INCOME IN JUNE. INCREASE IN U.S. SHORT-TERM INTEREST RATES HAS PUT UPWARD PRESSURE ON CANADIAN RATES. END SUMMARY.

2. EXCHANGE RATE: CANADIAN DOLLAR EXCHANGE RATE CONTINUED TO SAG UNDER STRONG SELLING PRESSURE DURING WEEK.

DOLLAR HAD SLUMPED FROM 87.78 U.S. CENTS TO 87.37 U.S. CENTS WITH ANNOUNCEMENT ON AUGUST 25 OF CDOLS 98 MILLION MERCHANDISE TRADE DEFICIT IN JULY. MARKET CONTINUED TO REACT TO DISAPPOINTING TRADE NEWS ON MONDAY, AUGUST 28 AS DOLLAR SLIPPED TO 87.05 U.S. CENTS. TOWARD MID-WEEK, PROFIT-TAKING AND PURCHASES OF DOLLARS TO COVER PREVIOUS SHORT SALES PROVIDED SHORT-LIVED SUPPORT TO DOLLAR BEFORE SELLING PRESSURE RESUMED DRIVING EXCHANGE RATE AS LOW AS 86.77 U.S. CENTS.

3. DEMAND FOR U.S. DOLLARS BY CANADIAN SUBSIDIARIES TO MEET END-MONTH PAYMENTS TO THEIR PARENTS AND RISE IN U.S. FEDERAL FUNDS AND PRIME RATES, NARROWING DIFFERENTIAL BETWEEN SOME CANADIAN AND U.S. SHORT-TERM RATES, ALSO HELPED TO WEAKEN CANADIAN DOLLAR (SEE PARA 10 BELOW).

4. OFFICIAL INTERNATIONAL RESERVES: DEPRECIATION OF CANADIAN DOLLAR IN RECENT WEEKS HAS OCCURRED DESPITE HEAVY OFFICIAL INTERVENTION TO SUPPORT EXCHANGE RATE. OFFICIAL INTERNATIONAL RESERVES DECLINED BY U.S.DOLS 398.4 MILLION TO U.S.DOLS 4.2 BILLION IN AUGUST. NET CHANGE IN RESERVES INCLUDED ADDITION TO FOREIGN EXCHANGE RESERVES OF U.S.DOLS 300 MILLION FROM DRAWINGS UNDER GOC STANDBY CREDIT WITH U.S. BANKS. THUS, INTERVENTION TO SUPPORT DOLLAR TOTALED U.S.DOLS 698.4 MILLION IN MONTH. DRAWINGS OUTSTANDING UNDER U.S.DOLS 3.0 BILLION STANDBY CREDIT WITH U.S. BANKS
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AND U.S.DOLS 2.5 BILLION STANDBY WITH CANADIAN BANKS NOW TOTAL U.S.DOLS 1.0 BILLION AND U.S.DOLS 500 MILLION RESPECTIVELY.

5. COMPOSITION OF OFFICIAL RESERVES (MILLIONS OF U.S. DOLLARS) ON AUGUST 31 WAS AS FOLLOWS (CHANGE FROM JULY 31 SHOWN IN BRACKETS): U.S DOLLARS, 2,081.2 MILLION (MINUS 407.3); OTHER FOREIGN CURRENCIES, 15.9 (MINUS 3.7); GOLD 978.3 (PLUS 8.4); SDR'S, 512 (PLUS 4.4); RESERVE POSITION IN IMF, 606.3 (MINUS 0.3); TOTAL 4,189.9 (MINUS 398.4).

6. ECONOMIC POLICY: ON SEPTEMBER 1, MINISTER OF EMPLOYMENT AND IMMIGRATION CULLEN REVEALED DETAILS OF CUTS IN UNEMPLOYMENT INSURANCE COMPENSATION (UIC) PAYMENTS AND INCREASED SPENDING ON JOB CREATION PREVIEWED IN AUGUST 24 SPEECH BY FINANCE MINISTER CHRETIEN (SEE OTTAWA 4213 AND 4230). CUTS IN UIC PAYMENTS WILL MAINLY AFFECT REPEAT CLAIMANTS AND NEW ENTRANTS INTO LABOR FORCE. INCREASED SPENDING ON JOB CREATION WOULD PRODUCE 113,000 "WORK YEARS" OF EMPLOYMENT AND WOULD INVOLVE 368,000 PERSONS IN WORK OR TRAINING.

7. TOURISM: TASK FORCE ON TOURISM SECTOR, ESTABLISHED AT FEDERAL/PROVINCIAL ECONOMIC SUMMIT IN FEBRUARY 1978, HAS ISSUED REPORT, BLAMING, INTER ALIA, HIGH COSTS IN CANADA RELATIVE TO U.S., AND "ENDLESS GOVERNMENT REGULATION" FOR CONTINUING INCREASE IN CANADIAN TRAVEL DEFICIT. REPORT ESTIMATES THAT SPENDING BY U.S. TOURISTS ABROAD WILL DOUBLE BY 1985 AND THAT CDOLS 5 BILLION OF NEW INVESTMENT WILL BE NECESSARY IF CANADA IS TO MAINTAIN ITS 20 PERCENT SHARE OF U.S. TRAVEL SPENDING. TASK FORCE CALLS FOR TAX INCENTIVES TO SPUR INVESTMENT AND URGES GOC TO "THINK TOURISM." (COPIES OF REPORT HAVE BEEN POUCHED TO WASHINGTON.)

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8. SECOND QUARTER GNP GROWTH: REAL GNP GREW AT SEASONALLY ADJUSTED ANNUAL RATE OF 4.4 PERCENT IN SECOND QUARTER, UP FROM 2.9 PERCENT RATE RECORDED IN FIRST QUARTER. PATTERN OF GROWTH EMPHASIZED DOMESTIC DEMAND, PARTICULARLY PRIVATE INVESTMENT, WHILE EXTERNAL SECTOR HAD NEGATIVE IMPACT ON GROWTH DUE TO SHARP REDUCTION IN TRADE SURPLUS (SEE OTTAWA 4249).

9. ECONOMIC INDICATORS:

--SEASONALLY ADJUSTED LABOR INCOME WAS CDOLS 10.9 BILLION IN JUNE, UP BY 1.4 PERCENT FROM MAY AND BY 9 PERCENT FROM JUNE 1977. SINCE CONSUMER PRICES ROSE BY 9.2 PERCENT IN TWELVE MONTHS TO JUNE LABOR INCOME DECLINED IN REAL TERMS OVER THIS PERIOD.

--INCREASE IN EMPLOYMENT, AVERAGE EARNINGS, AND HOURS WORKED CONTRIBUTED TO 1.4 PERCENT ADVANCE IN NOMINAL LABOR INCOME BETWEEN MAY AND JUNE. EMPLOYMENT INDEX (SA) ADVANCED BY 0.3 PERCENT TO 145.1 (1961=100). AVERAGE WEEKLY EARNINGS (SA) ROSE BY 1 PERCENT TO CDOL\$ 266.72
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WITH INCREASES RECORDED IN ALL SECTORS EXCEPT CONSTRUCTION. AVERAGE WEEKLY HOURS (SA) ROSE IN MINING, BUT DECLINED IN MANUFACTURING AND CONSTRUCTION. NOMINAL LABOR INCOME ROSE AT SEASONALLY ADJUSTED ANNUAL RATE OF ABOUT 2 PERCENT IN SECOND QUARTER, AS NOMINAL LABOR INCOME ADVANCED AT 11 PERCENT ANNUAL RATE, AND CONSUMER PRICES AT 9 PERCENT ANNUAL RATE.

--INDEX OF INDUSTRY SELLING PRICES (NSA) ROSE 0.3 PERCENT TO 187.9 (1971=100) IN JULY AND STOOD 7.3 PERCENT ABOVE ITS LEVEL OF JULY 1977. INDEX OF FOOD AND BEVERAGE PRICES DECLINED IN MONTH INDICATING THAT CONSUMERS MAY SOON GET SOME RELIEF FROM BURGEONING FOOD PRICES. HIGHER PRICES FOR PRIMARY METALS, TEXTILES AND CHEMICAL PRODUCTS HELPED BOOST INDEX IN JULY.

10. CAPITAL MARKETS: INCREASE IN U.S. SHORT-TERM INTEREST RATES HAS PUT UPWARD PRESSURE ON CANADIAN RATES. INTEREST RATES ON THREE-MONTH COMMERCIAL PAPER AND ON BANKERS' ACCEPTANCES ROSE BY 25 AND 10 BASIS POINTS RESPECTIVELY IN WEEK. INTEREST RATE ON THREE-MONTH TREASURY BILLS REMAINED CONSTANT, HOWEVER, AT 8.80 PERCENT DUE TO OPEN MARKET SALES OF TREASURY BILLS BY BANK OF CANADA. AS A RESULT, DIFFERENTIAL BETWEEN CANADIAN AND U.S. INTEREST RATES ON THREE-MONTH TREASURY BILLS NARROWED TO 132 BASIS POINTS IN WEEK FROM 158 BASIS POINTS PREVIOUS WEEK. WITH CANADIAN CHARTERED BANKS' PRIME RATE AT 9.75 PERCENT, DIFFERENTIAL WITH U.S. PRIME HAS DROPPED TO 50 BASIS POINTS. ENDERS

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